APPENDIX A

Opinion of the New York State Court of Appeals (Dated June 17, 1982)

COURT OF APPEALS

STATE OF NEW YORK

In the Matter of the Application of

Split Rock Nursing Home,

Petitioner,

For a Judgment Pursuant to Article 78 of the Civil Practice Law and Rules

against

The Office of Health Systems Management of the Department of Health of the State of New York, the Hon. David Axelrod, M.D., Commissioner of Health of the State of New York, Richard A. Berman, Director of the Office of Health Systems Management,

Respondents.

On review of submissions pursuant to Rule 500.2(b), judgment insofar as appealed from by State respondents, reversed, without costs, and order of Director of Office of Health Management Systems reinstated as it pertained to petitioner's incentive allowance. The Director of the Office of Health Management Systems did not act arbitrarily or unreasonably in this case in disallowing petitioner's incentive allowance for the years at issue. Accordingly, the determination of the Director must be sustained (*Matter of Cortlandt Nursing Care Center* v. *Whalen*, 46 N.Y.2d 979).

Chief Judge Cooke and Judges Jasen, Gabrielli, Jones, Wachtler, Fuchsberg and Meyer concur.

APPENDIX B

Order of the Appellate Division, Third Department (Entered January 6, 1982)

At a Term of the Appellate Division of the Supreme Court of the State of New York, held in and for the Third Judicial Department in the City of Albany, New York, commencing on the 5th day of October, 1981.

Present:

Hon. T. Paul Kane — Justice Presiding,
Hon. Robert G. Main
Hon. Ann T. Mikoll
Hon. Paul J. Yesawich, Jr.
Hon. J. Clarence Herlihy — Associate Justices.

County Clerk's Index No. 517/80

In the Matter of the Application of

Split Rock Nursing Home,

Petitioner,

For a Judgment Pursuant to Article 78 of the Civil Practice Law and Rules

against

The Office of Health Systems Management of the Department of Health of the State of New York, the Hon. David Axelrod, M.D., Commissioner of Health of the State of New York, Richard A. Berman, Director of the Office of Health Systems Management,

Respondents.

Appendix B

Order of the Appellate Division, Third Department

The above-named petitioner having instituted this proceeding in Supreme Court, Albany County, pursuant to article 78 of the Civil Practice Law and Rules, to review a determination of respondents, dated January 30, 1980, and said proceeding having been transferred for disposition to the Appellate Division, Third Department, by order of the Supreme Court, Albany County, dated April 11, 1980 and entered in Albany County, and having been presented during the above-stated term of this court and having been argued by David B. Bernfeld, Esq., of counsel for petitioner and by Joseph Micare, Esq., of counsel for respondents, and, after due deliberation the Court having rendered a decision on the 17th day of September, 1981, it is hereby

ORDERED that the determination be modified, by annulling so much of the order of the Commissioner of Health as disallowed petitioner's incentive alowance, and as so modified, confirmed, with costs to petitioner.

ENTER:

JOHN J. O'BRIEN
Clerk

DATED AND ENTERED: January 6, 1982.

A TRUE COPY
/s/ JOHN J. O'BRIEN
Clerk

APPENDIX C

Opinion of the Appellate Division, Third Department

SUPREME COURT
APPELLATE DIVISION
THIRD JUDICIAL DEPARTMENT

December 17, 1981. 40400

In the Matter of SPLIT ROCK NURSING HOME,

Petitioner,

v.

THE OFFICE OF HEALTH SYSTEMS MANAGEMENT OF THE DEPARTMENT OF HEALTH OF THE STATE OF NEW YORK et al.,

Respondents.

Proceeding pursuant to CPLR article 78 (transferred to this court by order of the Supreme Court at Special Term, entered in Albany County) to review a determination of the Commissioner of Health, which reduced petitioner's Medicaid reimbursements for the years 1972 and 1973.

Petitioner is a private nursing home located in the Bronx, New York, having opened for business in February, 1971. Its reports to the New York State Department of Health (Department) for the year 1971 established a prima facie basis for the grant of an "incentive allowance" pursuant to former section 86.31 of the Administrative Rules

and Regulations (10 NYCRR 86.31, repealed October 14, 1975). This section provided as follows:

> 86.31 Incentive allowance; proprietary nursing homes. Within the rate of payment for proprietary nursing homes, an amount may be included as an allowable cost which is equal to a percentage established by the Commissioner to represent a sharing in the amount by which the total costs of administrative, dietary and housekeeping services of an individual facility are lower than the weighted average ceiling of the costs of these services for the group. In instances where the latest survey disclosed significant deficiencies in the operation of a facility, the incentive allowance will not be available.

Based upon an audit of 1971 operating costs, petitioner was granted an incentive allowance for the rate period effective July 1, 1972 through December 31, 1972, and, after a change in its fiscal year, for the period of January 1, 1973 to December 31, 1973. As a result of an audit report dated November 11, 1975, adjustments were made by the Department auditors, effecting a reduction in the Medicaid reimbursement for those years as well as a reversal of the incentive allowance.

Petitioner protested the reduction in its reimbursement rates (enforced by withholding sums of approximately $350,000 from petitioner in 1978) and a hearing was held in 1978. Following that hearing on the audit reductions, petitioner abandoned its claim of error as to many of the various accounting deficiencies charged to it upon the audit. However, petitioner continued to protest the disallowance of the incentive allowance and the finding that the reim-

bursement rate for the period at issue should be based upon petitioner's actual costs for 1971. It is those two items that petitioner continues to contest in this proceeding.

As to the use of actual 1971 costs for setting the rate used in the period of July 1, 1972 through December 31, 1973, the Director of the Office of Health Systems Management (Director) computed the utilization factor at 98.4%. Petitioner has failed to establish any mathematical error or legal error as to this issue.

As to the disallowance of the incentive allowance, the Director found:

> [t]hat certain personal expenses of the operator and patients' personal monies were included in the working capital and hence the equity of the facility for reimbursement purposes, and upon audit disallowed, it is the Director's conclusion that the Respondent's action in so including them were significant deficiencies in the operation of the facility, as described in § 86.31. The use of patient monies to enhance one's return on equity by improperly using that money to inflate a nursing home's equity is not a proper use of the patient's personal monies. An audit, such as performed by Mr Kern is a survey within the meaning of § 86.31, as the term "survey" is synonymous with the term "inspection" as set forth in Public Health Law § 2803(1)(b). Hence, the incentive allowance should not be available to * * * [petitioner].

An agency interpretation of its own regulation is entitled to great weight and will be upheld if not irrational or reasonable (e.g., *Matter of Johnson* v. *Joy*, 48 N Y 2d 689; *Matter of Bernstein* v. *Toia*, 43 N Y 2d 437). The testimony

adduced at the hearing made it clear that in 1971 the policy of respondent was to disallow incentive allowances only if a facility was on the significant operating deficiency list. Although one witness did testify that some time after 1974 the commissioner decided that incentive allowances should also be lost if an audit disclosed improprieties in a facility's record keeping, no memorandum or other writing was produced disclosing this change of position. In fact, the only writing describing respondent's new "interpretation" of section 86.31 is the commissioner's order in this case dated January 30, 1980, four years after repeal of the regulation and two years after petitioner first protested respondent's action.

Testimony at the hearing disclosed that surveys of the nursing homes were conducted by regional health directors to identify those facilities providing less than adequate care. Any facility so identified was not eligible for an incentive award. Respondent's construction of "significant deficiencies in the operation of the facility" to include improprieties in the record keeping of the nursing home is not supported by any administrative precedent, written or otherwise. Thus, it should be rejected and petitioner's incentive allowance restored.

Determination modified, by annulling so much of the order of the Commissioner of Health as disallowed petitioner's incentive allowance, and, as so modified, confirmed, with costs to petitioner.

KANE, J.P., MAIN, MIKOLL, YESAWICH, JR. and HERLIHY, JJ., concur.

APPENDIX D

Order of Richard A. Berman, Director, Office of Health Systems Management

(Dated January 30, 1980)

STATE OF NEW YORK

DEPARTMENT OF HEALTH

OFFICE OF HEALTH SYSTEMS MANAGEMENT

IN THE MATTER

OF

SPLIT ROCK NURSING HOME

Request pursuant to Section 86-2.7, Chapter II of the Code of Rules and Regulations of the State of New York

To: Split Rock Nursing Home
3525 Baychester Road
Bronx, New York 10466

Robert Dobrish, Esq.
Hoffinger, Friedland and Roth
10 East 53rd Street
New York, New York 10022

A hearing in the above matter having been held before Francis P. Mulderry, Esq, hearing officer designated pursuant to the Public Health Law of the State of New York,

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Order of Richard A. Berman, Director, Office of Health Systems Management

and such hearing having been held on September 28, November 20, and December 5, 1978 in the hearing room of the Department of Health, Office of Health Systems Management, Nelson A. Rockefeller Empire State Plaza, Albany, New York and the World Trade Center 2, New York, New York; Office of Health Systems Management having appeared by Jerome T. Levy, Esq., and Melinda A. Bass, Esq., Counsel, Steven U. Teitlebaum, Esq., and Harriet Katz, Esq., of Counsel, the facility appeared by Hoffinger, Friedland and Roth, Robert Z. Dobrish, Esq., of Counsel, and transcripts of the proceeding having been made and exhibits received in evidence, and a hearing officer's report dated July 27, 1979, having been submitted, a copy of which is attached hereto, and made a part of this Order.

The Director adopts the Hearing Officer's findings of fact, opinions and recommendations as his own, with the following two exceptions:

A) In regard to the issue of basing a reimbursement rate on 1971 costs, the Director notes an additional finding of fact, in that the utilization factor was 98.4% (transcript pg. 122). In view of the fact that the utilization was over 90%, the Director hereby finds that the use of the cost report was proper in establishing a medicaid rate of reimbursement. This supplants the finding of fact noted by the hearing officer, to wit:

> "For 1971, Split Rock Nursing Home was slightly less than 90% capacity; i.e., 89.2% according to testimony of Ms. Wall. (Min. 11/20/78, p. 121)

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B) The Hearing Officer's findings of fact in regard to the issue of the incentive allowance was as follows:

"Ms. Wall of the Health Department testified that an incentive allowance is granted to facilities operating without deficiencies at a cost below group average. (Min. 11/20/78, pp 87-8)

"Terry Opela is a fiscal analyst employed by the New York State Department of Health and has been so employed for some 5½ years. (Min. 12/3/78, pp 177-8)

"Mr. Opela stated that incentive allowances would be forfeited if the facility was placed on the "significant operating deficiency list". (Min. 12/5/78, pp 192-3)

"The Hearing Officer deduces that both parties concede Split Rock Nursing Home was originally granted an incentive allowance.

"Mr. Kern, Department's witness stated that elimination of incentive allowances is not an audit function. (Min. 11/20/78, p. 166)

"Ms. Wall testified that there were no regulations with respect to removal of an incentive allowance based upon audit, but she indicated a memorandum exists which says an incentive allowance may be removed if an audit shows personal expenses were included in the report. (Min. 11/20/78, pp 47-8)

The Director's additional finding of fact is based on testimony during cross examination on the subject of the incentive allowance from pp 88-91. The additional finding of fact is as follows:

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Order of Richard A. Berman, Director, Office of Health Systems Management

Ms. Wall, testified at page 48:

Q. No. What I mean is: There is, as I understand it, a regulation that says that a retroactive adjustment can be made by the Department based on an audit?

A. That's true.

Q. Is there any regulation, rule, procedure, memorandum or anything that you know about that states that an adjustment can be made on anything other than an audit?

A. There is a memorandum that says that the incentive can be taken out if the home—if the audit shows that there were personal expenses in the report.

Q. If the audit shows that there were personal expenses?

A. Yes.

Q. That would be based on the audit; wouldn't it?

A. Right, as far as I know it's all based on the audit.

Q. So that any adjustment that's made not based on an audit would have no authority for it, would it?

A. Not that I know of.

Additionally, Ms. Wall testified on page 90 that an incentive allowance could be lost on audit. While Ms. Wall testified at page 88, line 11, that she thought that § 86.31 referred to "significant operating deficiencies," § 86.31 actually stated as follows:

"86.31 Incentive allowance; proprietary nursing homes. Within the rate of payment for proprietary nursing homes, an amount may be included as an allowable cost which is equal to a percentage established by the Com-

missioner to represent a sharing in the amount by which the total costs of administrative, dietary and housekeeping services of an individual facility are lower than the weighted average of the costs of these services for the group. In instances where the latest survey disclosed significant deficiencies in the operation of a facility, the incentive allowance will not be available."

This regulation remained in existence until October 14, 1975.

Mr. Opela (pg. 192-3) was aware of one aspect of losing the incentive allowance, that is the significant operating deficiency list. However, § 86.31 speaks of significant deficiencies in the operation of a nursing home, which would include a broader scope of activity.

In view of the Hearing Officer's finding of fact that in regard to Issue number 20 from the Notice of Hearing, that certain personal expenses of the operator and patients' personal monies were included in the working capital and hence the equity of the facility for reimbursement purposes, and upon audit disallowed, it is the Director's conclusion that the Respondent's action in so including them were significant deficiencies in the operation of the facility, as described in § 86.31. The use of patient monies to enhance one's return on equity by improperly using that money to inflate a nursing home's equity is not a proper use of the patient's personal monies. An audit, such as performed by Mr. Kern is a survey within the meaning of § 86.31, as the term "survey" is synonymous with the term "inspec-

tion" as set forth in Public Health Law § 2803(1)(b). Hence, the incentive allowance should not be available to Mr. Zelmanowicz.

The opinion of the Hearing Officer is stated as follows:

OPINION

"No Health Department regulations were in effect with respect to removal of incentive allowances other than for operating deficiencies. Internal correspondence referred to on this point did not exist during the year in question at this hearing.

"Therefore, it is the feeling of the Hearing Officer that removal of the incentive allowance was improper and it should be restored."

The Director overrules the Hearing Officer's conclusion that there was no regulation in effect with respect to removal of incentive allowances other than for operational deficiencies. In so doing, the Director takes official notice of 10 NYCRR 86.31 and Public Health law § 2803(1)(b).

C. UNCONTESTED ITEMS

Comissioner's Findings of Fact

The facility did not contest the following items from the Notice of Hearing:

"#3: Whether interest of $249. should not have been offset against investment income." The audit report had offset the $249. against the investment income.

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Order of Richard A. Berman, Director, Office of Health Systems Management

"#4: Whether legal expenses of $2,503. is allowable." The audit report had isallowed the $2.503.

"#5: Whether office expenses of $7,408. is allowable." The audit report had disallowed $3,418. of promotional advertising and capitalized $3,990. of movable equipment rather than expensing it.

"#6: Whether $228. of miscellaneous expense is allowable." The audit report had disallowed the $228.

"#7: Whether $722. of phone calls is allowable." The audit report had disallowed the $722.

"#8: Whether conference expenses of $1,632. is allowable." The audit report had disallowed the $1,632.

"#10: Whether kitchen suppplies of $3,134. should have been expensed." The audit report capitalized the $3,134.

"#11: Whether $6,140. of laundry expense is allowable." The audit report had disallowed the $6,140.

"#12: Whether $36,282. in repair and maintenance are allowable." The audit report treated it as follows:

> Costs (as per schedule H of the audit report) that should have been capitalized rather than expensed $10,435.
>
> Non-moveable equipment that should have been capitalized rather than expensed $19,988.
>
> Moveable equipment that should have been capitalized rather than expensed $1,765.

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1972 costs that were prepaid and hence disallowed upon audit $2,530.

Costs for which there had been an insurance recovery $220.

Personal expenses of the operators $1,344.

"#13: Whether $805. as light and power items are allowable as expense items." The audit report disallowed $447. and capitalized $358., rather than expensing it.

"#14: Whether $265. of personal expenses is allowable." The audit report had disallowed the $265.

"#15: Whether $7,724. in building supplies is allowable as expense items." The audit report capitalized the $5,843., rather than expensing it, and disallowed $1,881. of personal expenses of the operator.

"#16: Whether $4,270. of gardening expenses are allowable as expense items." The audit report capitalized $4,000. rather than expensing it, and disallowed $270. of personal expenses of the operator.

"#17: Whether $13,402. in medical supplies are allowable as expense items." The audit report capitalized $11,628. of moveable equipment rather than expensing it, and disallowed the following items:

Unallowable charges for prescription drugs	$1,216.
Unallowable charges for lab fees and doctors	141.
Personal expenses of operator	417.
Total	$1,774.

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Order of Richard A. Berman, Director, Office of Health Systems Management

"#18: Whether $7,713. of activities program is allowable as expense items." The audit report capitalized $3,494. rather than expensing it, and disallowed $4,219.

"#21: Whether $96,222. of the moveable equipment component of the basis for return on equity is allowable." The audit report had disallowed the net effect of $96,222. as part of the basis for return on equity.

CONCLUSION

In view of the concession by Split Rock Nursing Home and no evidence having been submitted by the facility, the audit adjustments should be sustained.

Now, upon the reading and filing of the Notice of Hearing and the Hearing Officer's findings of fact, opinion and recommendation, the Director

HEREBY ORDERS:

1. That in regard to Issue number 1 from the Notice of Hearing, administrative salaries shall be reduced by $17,780.00.

2. That in regard to Issue number 2 from the Notice of Hearing, payments to private duty nurses in the amount of $2,417.00 shall be disallowed.

3. That in regard to Issue number 9 from the Notice of Hearing, allowable automobile expenses shall be reduced by $6,019.00.

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Order of Richard A. Berman, Director, Office of Health Systems Management

4. That in regard to Issue number 19 from the Notice of Hearing, petty cash expenditures shall be reduced by $8,700.00.

5. That in regard to Issue number 20 from the Notice of Hearing, the working capital shall be reduced by $270,540.00.

6. That in regard to Issue number 22, the imputed rental allowance shall be that set upon audit of $313,407.00.

7. That the incentive allowance originally granted shall not be allowed.

8. That basing the reimbursement rate on 1971 costs was proper.

9. That in regard to Issue number 3, $249.00 of interest shall be offset against investment income.

10. That in regard to Issue number 4, $2,503.00 of legal expenses shall be disallowed.

11. That in regard to Issue number 5, $3,418.00 of promotional advertising shall be disallowed, and $3,990.00 of moveable equipment expense shall be capitalized rather than expensed.

12. That in regard to Issue number 6, $228.00 of miscellaneous expense shall be disallowed.

13. That in regard to Issue number 7, $722.00 of phone expense shall be disallowed.

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Order of Richard A. Berman, Director, Office of Health Systems Management

14. That in regard to Issue number 8, $1,632.00 of conference expenses shall be disallowed.

15. That in regard to Issue number 10, $3,134.00 of kitchen supplies shall be capitalized, not expensed.

16. That in regard to Issue number 11, $6,140.00 of laundry expense shall be disallowed.

17. That in regard to Issue number 12, $36,282.00 in repairs and maintenance shall be treated as follows:

Costs that shall be capitalized rather than expensed $10,435.00.

Non-moveable equipment that shall be capitalized rather than expensed $19,988.00.

Moveable equipment that shall be capitalized rather than expensed $1,765.00.

1972 costs that were prepaid and hence are disallowed $2,530.00.

Costs for which there had been an insurance recovery and hence are disallowed $220.00.

Personal expenses of the operator shall be disallowed $1,344.00.

18. That in regard to Issue number 13, $358.00 of light and power items shall be capitalized, not expensed; and $447.00 is disallowed.

19. That in regard to Issue number 14, $265.00 of personal expenses shall be disallowed.

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Order of Richard A. Berman, Director, Office of Health Systems Management

20. That in regard to Issue number 15, $5,843.00 in building supplies shall be capitalized, not expensed; and $1,881.00 of personal expenses of the operator shall be disallowed.

21. That in regard to Issue number 16, $4,000.00 of gardening expenses shall be capitalized rather than expensed; and $270.00 of personal expenses shall be disallowed.

22. That in regard to Issue number 17, $11,628.00 of medical supplies shall be capitalized, not expensed; and $1,774.00 of various items referred to in the findings of fact shall be disallowed.

23. That in regard to Issue number 18, $3,494.00 of activities program shall be capitalized, not expensed; and $4,219.00 shall be disallowed.

24. That in regard to Issue number 21, $96,222.00 of the moveable equipment shall not be a component of the basis for a return on equity.

It is further ORDERED:

That a rate of reimbursement be promulgated reflecting readjustments as per this Order.

Dated: Albany, New York
January 30, 1980

/s/ RICHARD A. BERMAN

Richard A. Berman, Director
Office of Health Systems Management

APPENDIX E

Report of Francis P. Mulderry, Hearing Officer and Commissioner's Representative

STATE OF NEW YORK

DEPARTMENT OF HEALTH

OFFICE OF HEALTH SYSTEMS MANAGEMENT

IN THE MATTER

OF

SPLIT ROCK NURSING HOME

Request pursuant to Section 86-2.7, Chapter II of the Code of Rules and Regulations of the State of New York

To: THE HON. DAVID AXELROD, M.D
Commissioner of Health of the State of New York;
and RICHARD A. BERMAN, Director of the Office
of Health Systems Management.

The Notice of Hearing dated August 25, 1978 with the statement of issues was duly served: the undersigned FRANCIS P. MULDERRY, ESQ., was duly designated as Hearing Officer; hearings were conducted on September 28, November 20 and December 5, 1978 in the Hearing Room of the Department of Health, Empire State Plaza, Albany, New York and Two World Trade Center, New York, New York;

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the Department of Health appeared by Jerome T. Levy, Esq., Counsel, by Harriet Katz, Esq. and Steven U. Teitelbaum, Esq. of Counsel, Respondent appearing by Hoffinger, Friedland & Roth, Robert Z. Dobrish, Esq. of Counsel, and transcripts of the proceedings were made and exhibits received in evidence.

Now, after due deliberation and consideration of the proceedings, the Hearing Officer does hereby submit his report including Issues, Findings of Fact, Opinion and Recommendations as follows:

BACKGROUND

The New York State Department of Health completed an audit report of the Split Rock Nursing Home for the period January 1, 1971 through December 31, 1971 with respect to reimbursement for Medicaid.

As a result of this audit report dated November 11, 1975 (Department Exhibit # 5), some adjustments were made by Department auditors, thus reducing the Medicaid reimbursement for those years.

The operators of Split Rock Nursing Home protested some of the adjustments made in the audit. The protest was reviewed by the Department's Rate Review Board after which certain items remain in dispute.

Pursuant to Section 2803 of the Public Health Law of the State of New York and Section 86-2.7, Chapter II of the Code of Rules and Regulations of the State of New

Appendix E

Report of Francis P. Mulderry, Hearing Officer and Commissioner's Representative

York, a hearing was held on the dates as herein stated to hear testimony with respect to the issues in dispute.

At the hearing of September 28, 1978, counsel for Split Rock Nursing Home requested that the issues of whether the 1971 costs as audited should form the basis for the rate in subsequent years, and whether an incentive award granted to the facility by the Department of Health should be eliminated. Counsel for the Department opposed this motion and as a result both parties stipulated to adjourn in order to obtain a court determination.

Justice Edward Conway of the New York State Supreme Court granted that counsel's request that the two additional issues should be heard and a decision rendered by the Hearing Officer on these issues as well as the audit issues.

Split Rock Nursing Home elected not to contest all of the items contained in the audit report which were originally protested leaving six items in contention which will be listed below by the number by which they were identified in the statement of issues attached to Exhibit # 2.

ISSUE I

Whether $17,780 in administrative salaries is allowable.

FINDINGS OF FACT

Marvin E. Kern is a Medical Facilities Auditor employed by the New York State Department of Health and has been employed as an auditor by the Department for approximately 12 years. (Min. 11/20/78, p. 137)

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Report of Francis P. Mulderry, Hearing Officer and Commissioner's Representative

Mr. Kern testified that the salary for Mr. William Brian had been charged partially to "other administrative salaries" because Mr. Brian was a nurse. (Min. 11/20/78, pp 143-4)

Mr. Kern's observations and discussions with Mr. Brian and the Nursing Home operator led him to a determination that Mr. Brian was functioning primarily as an assistant administrator. (Min. 11/20/78, pp 143-4-5-6)

The HE-2P filed by Split Rock Nursing Home listed William Brian as an assistant administrator. (Min. 11/20/78, p. 171)

Sidney Feld, present accountant for Split Rock Nursing Home testified that he was not familiar with Mr. Brian's duties or the allocation of his salary.

The transfer of Mr. Brian's salary to administrator's salaries had the effect of exceeding the ceiling for that item placed upon the facility by the Health Department.

OPINION

The audit adjustment with respect to the disallowance of the administrative salaries should be sustained.

ISSUE II

Whether $2,417 as payments to private-duty nurses is allowable.

FINDINGS OF FACT

The Health Insurance Manual-15 specifically precludes reimbursement of private-duty nurses, according to testimony of Mr. Kern. (Min. 11/20/78, p. 149)

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Mr. Kern, in making his audit report, noticed a disbursement category entitled "Non-ambulatory services". When he questioned the accountant and the operator, he was advised these sums were paid to private-duty nurses. (Min. 11/20/78, pp. 150-1)

Mr. Feld, Split Rock Nursing Home's accountant did not look at the books and records with respect to private-duty nurses and testified to his agreement that private-duty nurse payments are not reimbursable. (Min. 12/5/78, p. 231)

Mr. Kern's audit disallowed the sum of $2,417 in payments to private duty-nurses. (Exhibit # 5)

Opinion

The Nursing Home's testimony does not give the Hearing Officer any reason to do other than sustain the audit adjustment disallowing the $2,417 in payments.

Issue IX

Whether automobile expenses totaling $7,606 are allowable.

Findings of Fact

Mr. Kern, Department's auditor made an estimate of usage of automobiles by Split Rock Nursing Home based upon his operations while at the facility for a 60-day period. (Min. 11/20/78 pp 152-3)

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Mr. Kern stated that only auto expenses related to patient care are reimbursable according to regulations and HIM-15. (Min. 11/20/78, pp 156-7)

The allowance upon audit of 15 cents per mile was based upon the Internal Revenue Code at that time. (Min. 11/20/78, p. 157)

Split Rock Nursing Home had charged a total of $10,306 related to the use of automobiles, listed under various headings, such as medical expenses, kitchen supplies, etc. (Min. 11/20/78, p. 157)

In his audit, Mr. Kern estimated automobile usage for patient care based upon his operations and experience to be 1800 miles and allowed 15 cents per mile, for a total of $2,700, testifying that he was not provided with itemized expenses related to automobile usage.

Split Rock Nursing Home offered a detailed analysis of some of the automobile expenses which their accountant, Mr. Feld testified indicated a total of $4,287 in automobile expenses. (Exhibit G)

OPINION

The original amount of $10,306 was not documented by the Nursing Home. In the absence of documentation, Mr. Kern made an estimate from his operations over a short period of time. In view of the fact, Split Rock Nursing Home submitted some detail at the hearing, the Hearing Officer accepts this amount, thus the disallowance on audit should be $6,019.

Appendix E

Report of Francis P. Mulderry, Hearing Officer and Commissioner's Representative

Issue XIX

Whether $8,700 of petty cash expenditures should be allowable.

Findings of Fact

Mr. Kern's testimony was that Split Rock Nursing Home lacked documentation with respect to petty cash expenses. (Min. 11/20/78, pp 163, 169)

Further, it was stated by Mr. Kern that he discussed this matter with Mr. Newman, the previous accountant for the Nursing Home, and Mr. Feld, the current accountant, all of whom participated in a discussion which arrived at the amount of petty cash to be disallowed. (Min. 11/20/78, p. 163)

This was further discussed among the same parties plus the operator at the exit conference. (Min. 11/20/78, p. 165)

Split Rock Nursing Home offered no testimony which would lead the Hearing Officer to be swayed from Mr. Kern's determination.

Opinion

The audit adjustment with respect to the disallowance of petty cash should be sustained.

Issue XX

Whether $270,540 of working capital is allowable.

Appendix E

Report of Francis P. Mulderry, Hearing Officer and Commissioner's Representative

Findings of Fact

Disallowance on this point was made for three different reasons (See Exhibit # 5):

(a) Municipal bonds of the owners were a personal asset and thus not capital of the facility, totaling $236,198.

(b) Prepaid interest was adjusted to eliminate capital return on the non-current amount, a total of $28,532.

(c) Patients' personal monies were removed from return on capital since they should be a current liability, in the sum of $5,816.

Mr. Feld testified that it would not be proper to include personal bonds of the owner of a facility as working capital. (Min. 12/5/78, p. 232)

Further testimony elicited from Mr. Feld states that the patient monies were not capital of the facility. (Min. 12/5/78, p. 234)

At the hearing, both parties were silent with respect to prepaid interest. Mr. Kern's affidavit dated June 22, 1979, which was permitted to become part of the record due to misunderstanding at the hearing as to which items were uncontested, stated that interest from the bonds in question was not reflected in income of the Nursing Home, and the investment was not used as working capital.

Opinion

Overall testimony from both parties leads the Hearing Officer to the conclusion that the audit changes by the Health Department were proper as to the municipal bonds

and patients' personal monies, and there being nothing in the record to refute the decision on the prepaid interest, the adjustment with respect to reduction of working capital reimbursement is sustained.

Issue XXII

Whether $345,600 should be the imputed rental allowance rather than the $313,407 shown on the rate sheet.

Findings of Fact

During 1971, Split Rock Nursing Home was in operation for 331 days of the year. (Min. 12/5/78, p. 236)

Estelle Wall is a Fiscal Analyst employed by the New York State Department of Health who has served in that capacity for thirteen years. (Min. 11/20/78, pp 44-5)

Ms. Wall testified that imputed rental was calculated based upon the days of operation in 1971, which were 331. (Min. 11/20/78, p. 57)

The amount arrived at was a rate per day and would then be used in future years for the full term of the year, or 365 days at that rate. (Min. 11/20/78, pp 57-8)

Ms. Wall stated that this method of calculation, had it been made for a full 365 day year would have resulted in dividing by a larger number and the result would quite likely been almost the same. (Min. 11/20/78, p. 59)

Opinion

The Hearing Officer concedes that this is a very difficult point. However, the entire testimony indicates that the

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Health Department, in its audit, calculated imputed rental on a daily rate based upon the actual days of operation in 1971. Then this daily rate was used subsequently on a 365 day per year basis. Department's audit report in this respect should be sustained.

Incentive Allowance

It was the practise of the Health Department to grant an incentive allowance to those Nursing Homes whose rates were below the group average and which were being operated without significant operational deficiencies.

Findings of Fact

Ms. Wall of the Health Department testified that an incentive allowance is granted to facilities operating without deficiencies at a cost below group average. (Min. 11/20/78, pp 87-8)

Terry Opela is a fiscal analyst employed by the New York State Department of Health and has been so employed for some 5½ years. (Min. 12/5/78, pp 177-8)

Mr. Opela stated that incentive allowances would be forfeited if the facility was placed on the "significant operating deficiency list". (Min. 12/5/78, pp 192-3)

The Hearing Officer deduces that both parties concede Split Rock Nursing Home was originally granted an incentive allowance.

Mr. Kern, Department's witness stated that elimination of incentive allowances is not an audit function. (Min. 11/20/78, p. 166)

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Ms. Wall testified that there were no regulations with respect to removal of an incentive allowance based upon audit, but she indicated a memorandum exists which says an incentive allowance may be removed if an audit shows personal expenses were included in the report. (Min. 11/20/78, pp 47-8)

Opinion

No Health Department regulations were in effect with respect to removal of incentive allowances other than for operating deficiencies. Internal correspondence referred to on this point did not exist during the year in question at this hearing.

Therefore, it is the feeling of the Hearing Officer that removal of the incentive allowance was improper and it should be restored.

Issue

Should 1971 costs form the basis for the rate for ensuing years.

Findings of Fact

Split Rock Nursing Home was a new entity without adequate cost experience, which opened in early 1971 and was open 331 days in that year. (Min. 12/5/78, p. 236)

The facility submitted an HE-2P form at the conclusion of 1971 showing eleven months costs on a form designed for twelve months costs.

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For 1971, Split Rock Nursing Home was slightly less than 90% capacity; i.e., 89.2% according to testimony of Mr. Wall. (Min. 11/20/78, p. 121)

Under the rules in effect in 1971, new facilities without adequate cost experience were reimbursed at the lesser of group average or actual cost as determined by cost experience—6 months at 90%. The reason for this is to avoid windfalls to the facility by virtue of fixed expenses divided by an inadequate number of patient days.

Opinion

In order to control costs, the Health Department policy is to reimburse at the lower of group average cost or actual cost where a facility's past experience is inadequate.

Where there is less than 90% capacity and fewer than twelve months experience, the facility actually receives a benefit since ceilings are based on a full year and reimbursement is arrived at by dividing cost by patient days; i.e.,

A. Rental ceiling = X for twelve months.

B. If the facility pays rent for only ten months it has a benefit over the ceiling of approximately 16.7%.

To use the group average for reimbursement would create an incentive to increase costs rather than reduce them, therefore, the Health Department's decision to use 1971 costs as a basis for rates should be sustained.

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RECOMMENDATIONS

Based upon the above opinions, I recommend the following:

ISSUE I:—Administrative salaries should be reduced by $17,780.00

ISSUE II:—Payments to private duty nurses in the amount of $2,417.00 should be disallowed.

ISSUE IX:—Allowable automobile expenses should be reduced by $6,019.00

ISSUE XIX:—Petty cash expenditures should be reduced by $8,700.00.

ISSUE XX:—Working capital should be reduced by $270,540.00

ISSUE XXII:—The imputed rental allowance should be that set on audit.

INCENTIVE ALLOWANCE ISSUE:—The incentive allowance originally granted should be restored.

RATE BASIS ISSUE:—Basing the rate on 1971 costs was proper.

DATED: Albany, New York
July 27, 1979

Respectfully submitted,

/s/ FRANCIS P. MULDERRY

FRANCIS P. MULDERRY
Hearing Officer and
Commissioner's Representative